Supreme Court, U.S.
FILED
NOV 16 2004
OFFICE OF THE CLERK

(13)

No. 03-184

IN THE

Supreme Court of the United States

CLAUDE M. BALLARD AND MARY B. BALLARD,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

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REPLY BRIEF ON THE MERITS

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WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20001

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INTRODUCTION

The Rule 183(b) report represents the only record of the presumptively correct factual findings made independently by the only judicial officer to attend the trial and observe the testimony. Despite the obvious importance of the Special Trial Judge's ("STJ") fact-findings, the IRS argues that a copy of the Rule 183(b) Report need not be included with the record provided to reviewing Article III courts—including this Court. The IRS contends that reviewing Article III courts should be denied the ability to verify that the Tax Court's final opinion did treat the Rule 183(b) Report with "due regard" or review the basis for any actual "modification" or "rejection" of an STJ report. The Tax Court's insistence on keeping the original factfindings secret from both the Article III courts and the parties is plainly contrary to the statutory

and constitutional requirement of Article III review and departs so far from traditional American practice as to violate Due Process guarantees.

As it has throughout these proceedings, the IRS fails to distinguish between the Rule 183(b) Report that the Special Trial Judge is required to prepare and the opinion that is ultimately released by the Tax Court. There is ***only one*** Rule 183(b) Report: by statute and rule it is prepared by the STJ in the wake of the trial and submitted to the Chief Judge of the Tax Court. The STJ submits his Rule 183(b) Report *before* a Regular Tax Court Judge is assigned to the case, and this submission ends the STJ's participation in the case. Thereafter, a Regular Tax Court Judge may: (1) adopt the report; (2) modify it; or (3) hear additional testimony or argument. In this case, as in apparently ***every*** case decided by the Tax Court since the implementation of its current Rule 183 in 1984, the final record indicates only that the Rule 183(b) Report was "adopted." No reviewing Article III court has been permitted to determine whether the original factfinder's report was given the "regard" and deference that it is indisputably "due," as required by the text of the Rule, the command of Congress, and Due Process.

Contrary to the IRS's contention, the Rule 183(b) Report is in no way part of the Tax Court's internal deliberative process. Indeed, nowhere in the Tax Court's rules (or anywhere else, at least until the briefing in this case) is there any suggestion that the Rule 183(b) Report will be a "collaborative effort" or that its post-submission review will include the STJ's acceptance of any modifications made by the Regular Tax Court Judge. The IRS further argues, in the alternative, (i) that STJs and Regular Tax Court Judges are analogous to co-equal judges on a panel, jointly producing a decision, and (ii) that the relation of the STJ to the Regular Tax Court Judge is like that of a law clerk to a judge, or staff to the head of an administrative agency. As detailed in this brief and elsewhere, both of these analogies fail: the

employee-at-will STJs are not "peers" with the Regular Tax Court Judges, while law clerks do not preside at trial. But there is one proposition that cannot be disputed: STJs cannot be both equal participants with the Tax Court Judges, like members of the same appellate panel, and also subservient to them, like law clerks.

In the same statute that creates the Tax Court,[1] Congress has directed that the Article III courts of appeals review decisions from the Tax Court "in the same manner and to the same extent as decisions of the district courts," and this compels inclusion of the Rule 183(b) Report in the record. The IRS ignores the fact that the Article III district courts ***always*** include the factfinding from the trier of fact in the record. Congress requires no less of the Tax Court.

As part of its effort to perpetuate the secrecy surrounding the STJ's Rule 183(b) Report, the IRS makes several arguments that simply miss the mark:

- The right to a fair trial in a fraud case involving the personal reputations of individual taxpayers and millions of dollars is not subject to the reduced procedural protections associated with rate-making proceedings or other administrative matters. The IRS has cited no case to the contrary.
- No discovery from the Tax Court is necessary or will be sought. It is simply inaccurate to assert that Petitioners seek to invade the deliberative process of the Tax Court by deposing judges or serving written discovery. Petitioners merely seek the disclosure of the Rule 183(b) Report to the reviewing appellate courts on remand, and no discovery of any kind is necessary to achieve this result.[2]

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[1] 26 U.S.C. § 7482.

[2] Resp. Br. at 30. Far from being an improper invasion of the decisional process, the comparison of legal and factual conclusions is some-

- No finding of judicial misconduct is needed to resolve the question at hand. As with any question of fact or law, the Tax Court may err without engaging in any misconduct by denying the Rule 183(b) Report its presumption of correctness. The inclusion of the Rule 183(b) Report in the record is obviously necessary to guard against this sort of error, regardless of the presence or absence of judicial impropriety.
- This Court's grant of certiorari was not improvident, as no hypothetical future case could more perfectly frame the issue of whether the Rule 183(b) Report must be included in the record. Because the Tax Court *always* purports to "adopt" the STJ's Rule 183(b) Report and the STJ's Report is *never* included in the record, this issue could not reach this Court in any other posture.

ARGUMENT IN REPLY

I. BOTH CONGRESSIONAL COMMAND AND ARTICLE III REQUIRE INCLUSION OF THE RULE 183(b) REPORT IN THE RECORD.

A. Congress' Grant of Article III Review to the Taxpayers Necessitates Review "In the Same Manner and to the Same Extent" as Decisions from a Federal District Court.

The IRS has failed to answer the Petitioners' contention that the statutory command of Congress requires the inclusion of the Rule 183(b) Report in the appellate record. It is

thing that this Court and the courts of appeals regularly undertake in a variety of contexts. For example, this Court regularly examines whether a court of appeals applied the proper standard of review to a district court decision. The courts of appeals themselves regularly compare the factual conclusions reached by district judges to the factual conclusions reached by magistrates or bankruptcy judges.

undisputed that Congress has given taxpayers the right to have their Tax Court cases reviewed by Article III courts "*in the same manner and to the same extent* as decisions of the district courts in civil cases tried without a jury." 26 U.S.C. § 7482 (emphasis added).[3] Consistent with this statutory command, the striking parallel between the language of FED. R. CIV. P. 52(a) and TAX CT. R. 183(c) confirms that the STJ is the only possible trier of fact. In establishing the role of the district judge as the trier of fact in a bench trial, Rule 52(a) mandates that the judge's factfindings "shall not be set aside unless clearly erroneous, and ***due regard*** shall be given to the opportunity of the trial court to judge the credibility of the witnesses." (emphasis added).

Obviously, an Article III appellate court reviewing a decision from a bench trial before a district court has access to the findings of fact made by the district judge. Hence, in order to make possible appellate review of Tax Court decisions "in the same manner and to the same extent"[4] as decisions from a federal district judge, the STJ's Rule 183(b) Report must be included in the record. Thus, the only logical reading of the statute is that it calls for the reviewing Article III court to have access to the findings of the STJ before they are "modified" or "rejected." This is precisely the statutory construction that this Court adopted in *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 493 (1951). This construction pretermits the need for constitutional decision making, as is favored. *See DeBartolo Corp. v. Fla. Gulf Coast Bldg.*, 485 U.S. 568, 575 (1988).

[3] Because Congress has, by statute, given authority over tax cases to the Article III courts, the common law principles from the "court of the exchequer" invoked by the IRS (Resp. Br. at 38) are irrelevant. *See infra* at 13.

[4] 26 U.S.C. § 7482.

B. Article III Requires a Full Record for Meaningful Review.

It is well established that adjudication in an Article I court is valid only where recourse to appellate review in an Article III court is possible.[5] Meaningful Article III appellate review is, of course, entirely dependent on the existence of a full and complete record of the proceedings before the Article I court —and the availability of that record to the Article III court.

The Tax Court's refusal to provide the Article III courts with access to the factfindings of the trier of fact prevents valid Article III review.[6] Indeed, this Court has previously held that findings of fact from the Article I judge hearing the testimony are an essential part of the Article III appellate record: "Surely an examiner's report is as much a part of the record as the complaint or the testimony."[7]

II. THERE IS ONLY ONE RULE 183(b) REPORT, AND NO ARTICLE III COURT KNOWS WHAT IT SAID.

A. The Rule 183(b) Report Constitutes Presumptively Correct Factfindings.

Throughout these proceedings, the IRS has offered divergent, inconsistent, and entirely new explanations for the role of the STJ in the decision making process at the Tax Court.[8] However, as even a brief review of Tax Court Rule 183(b) reveals, the STJ's Report is a distinct, legally required

[5] Ballard's Br. at 24-25 & n. 18.

[6] Further, it is not the prerogative of the Article I trial court to dictate to the Article III appellate court the contents of the record that it will review.

[7] *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 493 (1951) (Frankfurter, J.) (The Court went on to declare that "reviewing courts" should "give to the examiner's report such probative force as it intrinsically commands.").

[8] Ballard's Br. at 17-22.

document authored exclusively by the STJ in the wake of trial and ***before*** a Regular Tax Court Judge is assigned to the case. The Rule 183(b) Report must be understood as the original factfinding in the case, and for that reason, is presumptively correct. Hence, no meaningful Article III appellate review is possible without access to the Report.

The IRS's shifting characterization of the role of the STJ notwithstanding, the Tax Court's use of an STJ under its Rule 183 to adjudicate a case involves several clear and distinct steps:

(1) The STJ is the only judicial officer present at the trial and presides;[9]

(2) Following trial and the submission of briefs from the parties, the STJ prepares his Rule 183(b) Report, containing his findings of fact and opinions of law;

(3) The STJ submits his Rule 183(b) Report to the Chief Judge of the Tax Court, thereby ending the STJ's participation in the case;

(4) Thereafter, the Chief Judge assigns the case to a Regular Tax Court Judge and forwards the STJ's Rule 183 Report to that Judge;

(5) The Regular Tax Court Judge is obligated to afford the findings of fact in the STJ's Rule 183(b) Report a presumption of correctness, but the Regular Tax Court Judge is ultimately responsible for preparing the Tax Court's opinion, and he may recall witnesses to assist him in doing so; and

[9] *Freytag v. CIR*, 501 U.S. 868, 881-82 (1991) (noting that as the lone judicial officer presiding at trial, the STJ has to power to "take testimony, conduct trials, rule on the admissibility of evidence, and . . . enforce compliance with discovery orders.").

(6) In preparing his opinion, the Tax Court Judge may "adopt" or "modify" or "reject in whole or in part" the STJ's Rule 183(b) Report, but he still remains obligated to give the STJ's Report "due regard" and to treat its factfindings as "presumptively correct."

In reviewing these steps, it becomes obvious that that there is only ***one*** Rule 183(b) report—the document prepared by the STJ after trial and submitted to the Chief Judge of the Tax Court. Thus, the IRS's insinuation that the Rule 183(b) Report is merely some sort of "draft" of the Tax Court's final decision is simply inaccurate.[10] Nor, contrary to the IRS's position, does the Rule 183(b) Report stem from any sort of "collaborative" effort between the STJ and the Regular Trial Judge. The STJ cannot, as a practical matter, collaborate with a Regular Tax Court Judge in the preparation of the Report because it is completed and submitted ***before*** the case is assigned to a particular Tax Court Judge. Moreover, the submission of the Rule 183(b) Report to the Chief Judge ends the STJ's role in the case, as no Tax Court rule or procedure provides for any sort of post-submission collaboration between the STJ and the Regular Tax Court Judge. Thus, properly understood, the Rule 183(b) Report is the legally required and exclusive final product of the STJ, who has no role in the case after he submits his Report.

The Regular Tax Court Judge's right to "modify" or "reject" the STJ's Rule 183(b) Report does not eliminate his obligation to give the Report "due regard" or to treat its factual conclusions as "presumptively correct." Indeed, the legal status of the Rule 183(b) Report as the original factfindings in the case is ultimately unaffected by the Regular Tax Court Judge's treatment of the Report. For example, if the Regular Tax Court Judge decides to "reject" or "modify" the Report's factfindings, it must be because the presumption

[10] Resp. Br. at 20, 24.

of correctness attached to those findings was properly overcome. Yet the Tax Court refuses to permit the Article III courts—including even this Court—to know whether the Regular Tax Court Judge decided to "reject" or "modify" the Report's factfindings, let alone to examine whether such action was proper. As it is, no Article III court is in a position to determine whether the Regular Tax Court Judge actually gave the Rule 183(b) Report the deference that it is indisputably owed.

To be sure, the Tax Court could, if it desired, refuse to employ STJs.[11] Instead, the Regular Tax Court Judges could simply conduct all trials themselves, with the assistance of law clerks. If that were the case, the law clerks' memoranda would not be publicly released, nor would they be given any official recognition as worthy of "due regard." At the other end of the spectrum—as Petitioners here suggest—the Tax Court can and should acknowledge that where the STJ is the sole judge who conducted the trial and viewed the witnesses, and where his official factfinding report is required by statute to be reviewed by a higher judge, that report should (at a bare minimum) be part of the record.

But here, by the IRS's argument, the Tax Court (1) should have the freedom and flexibility to allow a subordinate judge acting alone to conduct a trial, while (2) treating that judge's factfinding report as nothing more than the equivalent of a law clerk's preliminary memorandum. This is an unprecedented result. The Tax Court must make a choice: if it means to hire the equivalent of law clerks, it cannot assign trials to be solely conducted by them. But if it gives STJs the responsibility of conducting trials and finding facts based upon evidence, it must make their factfinding reports part of

[11] After all, Congress left it to the Chief Judge's discretion whether STJs will be employed or used. *See* 26 U.S.C. § 7443A.

the record, just as is done in every other context known to the American legal system.

B. The Regular Tax Court Judge's Opinion and the Rule 183(b) Report are Distinct, Regardless of Whether the STJ Ultimately "Joins" the Opinion.

The IRS has posited that the Regular Tax Court Judge and the STJ collaborated in the preparation of the final opinion, *i.e.*, that the STJ ultimately came to agree with or "join" Judge Dawson's opinion.[12] Thus, the IRS's argument goes, the underlying Rule 183(b) Report is reduced to irrelevance and need not be part of the appellate record.

But this argument fails to take into account that the Rule 183(b) Report contains the original and unmodified findings of fact from the only judicial officer present at trial, or to explain what value the absent-from-trial Tax Court Judge adds to the credibility determinations made by the STJ. Beyond this, there is no mechanism in the Tax Court Rules or elsewhere by which the STJ can concur with or dissent from any modifications or rejection of the Rule 183(b) Report. The STJ's post-submission statement purporting to "join" the Tax Court's final opinion has no legal value: it is the Rule 183(b) Report itself, not any after-the-fact statement by the STJ, that is "presumed to be correct."

By way of analogy, a jury's factfindings are not expunged from the record simply because a district judge issues a judgment as a matter of law and the jurors subsequently come to agree with the judge's reasoning. Nor does the fact that jurors changed their minds alter the standard of review applicable on appeal: the jury's original, uninfluenced, independent factfindings remain part of the record and remain entitled to substantial deference regardless of any juror's post-verdict

[12] Resp. Br. at 17-19.

change of heart. Just as a reviewing court of appeals must determine whether a district judge granting JMOL afforded proper deference to the jury's verdict, so too must the courts of appeals be allowed to confirm that the Tax Court properly gave deference to the STJ's Rule 183(b) Report.

C. The STJ Is the Only Possible Factfinder.

The IRS's only answer to the obvious need to include the Rule 183(b) Report in the record is to deny that the STJ is actually the finder of fact and to contend that, as such, his Report is merely an internal court document. In other words, the IRS envisions the "Special ***Trial Judge***" as something far less than a judge and more akin to a stenographer who takes notes on behalf of the absent actual factfinder, the Regular Tax Court Judge. Because the STJ's Rule 183(b) Report is, under the IRS's theory, more akin to a summary of the transcript or, at best, a law clerk's bench memo, it need not be included in the record.[13]

The IRS's argument ignores the reality of practice before the Tax Court. As the only official observer of the testimony, the STJ cannot be analogized to a law clerk, secretary, or other employee whose work is inherently internal in nature. The presumption of correctness that attaches to the Rule 183 Report flows not only from the explicit language of the Tax Court's own rule, but, more importantly, from the STJ's status as the only person on hand at trial to make credibility determinations.[14] Thus, the IRS's attempt to charac-

[13] Resp. Br. at 31-32. *Cf. Freytag v. CIR*, 501 U.S. 868, 881-82 (1991) (holding that STJs "perform more than ministerial tasks" and that "[i]n the course of carrying out these important functions, the special trial judges exercise significant discretion."). In light of this, the IRS appears to be making arguments in the present case that this Court rejected in *Freytag*.

[14] Such credibility determinations are, obviously, all the more important in a fraud case such as this, where the IRS must prove that "the peti-

terize[15] the STJ as anything other than the original finder of fact is disingenuous: there is simply no other *bona fide* candidate for the position.

III. THE *RADDATZ* PRINCIPLE APPLIES TO THIS FRAUD CASE.

Under this Court's precedents, credibility assessments made by a judge who observed the witnesses should rarely, if ever, be reversed on the basis of a cold record by a reviewing judge who was not present at trial. *See United States v. Raddatz*, 447 U.S. 667, 681 (1980); *Peretz v. United States*, 501 U.S. 923, 939 (1991).[16] This was a fraud case where credibility determinations were of vital importance. The dispositive credibility determinations were, by necessity, made by the only judicial officer present at trial—the STJ—and memorialized in his Rule 183(b) Report. Consistent with the *Raddatz* principle, Due Process demands that the credibility determinations in the Rule 183(b) Report be given substantial deference.

The IRS's argument against the applicability of *Raddatz* is flawed. Although this case is not a criminal prosecution, this tax fraud case is closer in form and consequence to a criminal matter than it is to the administrative proceedings concerning rulemaking, rate setting, or license applications invoked by the IRS.[17] As the liberty or property interest at issue increases, so does the level of Due Process protection that must be afforded.[18] Where, as here, a court's actions will "engender adverse social consequences to the individual" or result in

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tioner has been guilty of fraud with intent to evade tax" by "clear and convincing" evidence. 26 U.S.C. § 7454(a); TAX CT. R. 142(b).

[15] Resp. Br. at 31-32.

[16] Ballard's Br. at 32-35.

[17] Resp. Br. at 47-48.

[18] *Addington v. Texas*, 441 U.S. 418, 425-26 (1979).

a "stigma," an increased level of Due Process protection is warranted.[19] Thus, the elevated "clear and convincing" standard of proof applies. The imposition of significant monetary penalties[20] and other purely punitive measures upon Petitioners will accompany a finding of guilt. Moreover, in the business world, fraud carries with it a stigma akin to that of a criminal conviction, and here it is an individual, rather than any institution, who must personally bear that stigma.[21]

The IRS cites no case holding that an absent-from-trial judge is permitted to make factfindings in a quasi-criminal case such as this. Hence, while it may be constitutionally permissible for an absent-from-trial trier of fact to make findings in cases concerning livestock pricing[22] or other technical administrative matters, such absentee factfinding is unacceptable in the context of a fraud trial whose outcome

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[19] *Id.* at 426.

[20] The penalty for tax fraud is a fine of 75% plus interest for any tax deficiency attributable to fraud, plus payment of the underlying tax deficiency. 26 U.S.C. § 6663. Further, the fraud finding caused the statute of limitations not to apply, subjecting the Ballards to liability for tax years long past. 26 U.S.C. § 6501(c)(1). Hence, Petitioners' property interest at issue in this case was quite substantial.

[21] Because he was a well-respected and prominent business figure, the quasi-criminal stigma surrounding a finding of tax fraud has impacted Claude M. Ballard's life in multiple material and negative ways. For example, Mr. Ballard has been forced to resign from several boards of directors on which he formerly sat. His reputation has been damaged and he has endured various business and social consequences as a result of the Tax Court's finding of fraud. Mr. Ballard has endured this stigma, notwithstanding the fact that he reported income on which he paid over $6 million in federal income taxes in the years in question. *See* Trial Exhibits 385-93.

[22] Resp. Br. at 48-49 (relying heavily on *Morgan v. United States*, 298 U.S. 468 (1936), a pre-APA case concerning the Secretary of Agriculture's right to determine without personally hearing live testimony the maximum rate to be charged in the buying and selling of livestock).

hinges almost entirely on the credibility of witnesses. The STJ's apparent post-Report change of heart does not cure this problem.

IV. THE GOVERNMENT'S REMAINING ARGUMENTS FAIL.

Rather than repeat arguments made in other briefs, it is necessary only to note the flaws in several arguments raised by the IRS in the hopes of avoiding the merits of this issue altogether. Specifically, the IRS (1) implies that this case turns on some kind of judicial impropriety; and (2) that a reversal will somehow require or invite discovery from the Tax Court itself; and (3) that certiorari was improvidently granted. For the reasons detailed *supra* on pages three and four, these arguments are red herrings.

V. THE TAX SYSTEM IS UNDER THE PURVIEW OF THE ARTICLE III COURTS.

The IRS's desire to deny reviewing Article III courts access to the Rule 183(b) Report based, in part, on ancient common law "court of exchequer" practices[23] reflects the IRS's failure to recognize that Congress has placed the tax system under the purview of the Article III courts. Not only is the Tax Court subject to review by the Article III courts, the Tax Court itself has steadily evolved into a forum closely resembling a district court.[24] Yet the IRS apparently believes that the Tax Court is still immune to the strong public policy favoring judicial transparency.[25]

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[23] Resp. Br. at 38-39. Ballard's Br. at 46.

[24] Harold Dubroff, *The United States Tax Court: An Historical Analysis* (pts. 1-6), 40 ALB. L. REV. 7 (1975), 40 ALB. L. REV. 253 (1976), 41 ALB. L. REV. 1 (1977), 41 ALB. L. REV. 639 (1977), 42 ALB. L. REV. 161 (1978), 42 ALB. L. REV. 353 (1978).

[25] Ballard's Br. at 46.

Consistent with its evolution towards transparency and accountability, the Tax Court should not be allowed to conceal the factfindings in this or any other case. The IRS's invocation of English exchequer practice notwithstanding, Congress demands more of the Tax Court: meaningful Article III review, which requires the inclusion of the factfindings in the record. To hold otherwise is to permit a degree of secrecy otherwise unknown in the modern American legal system and wholly inconsistent with the Tax Court's transformation into a trial court more closely akin to the federal district courts.

CONCLUSION

For all of the foregoing reasons, the judgment of the court of appeals should be vacated in its entirety, and this case remanded for further proceedings consistent with this Court's opinion, including an order that the report of the Special Trial Judge be provided to the parties and made part of the appellate record.

Respectfully submitted,

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